Need to stabilise the GST tech platform

O N JULY 1 THIS year, Goods and Services Tax (GST) completed three years. It was on the midnight of July 1, 2017, that GST was unveiled with a lot of fanfare and hailed as a “good and simple tax”, “one country-one tax”, “game-changer” and “a reform of the century”. The implementation of a destination-based, standard-invoice-credit-type GST in a large and diverse federal country, at both the national and sub-national levels ruled by different political parties, was considered a remarkable achievement and a great experiment in cooperative federalism with both the Centre and state governments ceding fiscal autonomy to achieve a harmonised domestic consumption tax system in the country. More importantly, 100% invoice matching to verify input tax credit was supposed to enhance the compliance of the tax and the tax was expected to be a “money machine”.

However, three years after the implementation, not many are celebrating. Both the Centre and states are complaining about the shortfall in revenues. In FY20, the actual revenue collection from GST of central government was 24% lower than the budget estimate and 18% lower than the revised estimate. The revenue from the tax for FY21 is budgeted at ₹6.9 lakh crore, and it would require almost 40% growth to achieve this. Of course, Covid-19 has had a severe adverse impact on revenue collection, and even if last year’s revenue from the tax is collected, there will be a shortfall of almost ₹3 lakh crore from the budget estimate for FY21.

The aggregate revenue collection of Centre and states from GST (excluding the compensation cess) in the first quarter is 41% lower than the revenue collected during the corresponding period last year. In June, collections rose sharply to ₹90,917 crore after dismal collection of ₹32,294 crore in April, and ₹62,009 crore in May. It would, however, be too hasty to conclude that increased revenue collection is entirely due to economic recovery. Of course, this is partly due to lifting of the lockdown, but is also due to delayed filing of GST returns. The government allowed a relaxed time schedule for filing GST returns for March and April, and even some returns of February too got filed in June.

The states are staring at an uncertain future regarding the revenue from GST. They joined the GST reform on the promise of generous compensation of 14% increase every year over the revenue collected from the taxes subsumed in GST in FY17. Although there was an assurance by the Finance minister that the Centre will make the compensation payments even if it has to borrow when the collection from compensation cess falls short, the present finance minister, in her budget speech, has categorically stated, “Hereinafter, transfer to the (compensation) fund would be limited only to collection by way of GST compensation cess”. With the revenue productivity of GST continuing to be low and the promised compensation not forthcoming, states are faced with a serious dilemma; they cannot quit the GST regime and face serious revenue uncertainty. The revenue uncertainty is even more after the compensation agreement gets over in FY22.

The most important reform needed now is to rationalise the rate structure to minimise the number of rates. Excessive rate differentiation results in misclassification, anomalies, and inverted duty structure. There are at least seven rate categories in addition to cess on certain supplies at varying rates. The much talked about higher tax rate on ‘parasites’ is not an isolated matter. The differential tax rates on silk and jute (exempted), cotton and natural (5%), man-made fibres (18%) creates serious anomalies and inverted duty structure on blended fabrics. Rate differentiation is also done according to the stage of production (mineral products and their finished goods), value of the supply, hotels (footwear) and use of the commodity. Rationalisation of rates is important not only to simplify the tax to enable better compliance but also to avoid anomalies and inverted duty structures.

Reforming the rate structure of GST is important, but carrying that out, in the present juncture, may not be easy. First, the Centre itself should be convinced that rate rationalisation is important. Second, passing any reform of the structure would require 75% of the votes in the GST Council. The Centre has only one-third of the votes to carry and it needs to secure the support of at least 20 of the 31 states and Union Territories with legislature to get the reform passed in the Council. However, when the revenue is declining and with so much trust deficit, it is doubtful whether the GST Council will vote for substantial rationalisation in the rate structure. They may make minor changes, but drastic reduction in the number of rates may be difficult in the prevailing environment.

Serious reform of the tax structure is feasible only when there is promise of increase in revenue productivity. A major reason for low revenue productivity of the tax is its poor compliance. The most important reason for the failure to evoke better compliance of the tax, unlike in many countries, is the failure to stabilise the technology platform even after three years. The original idea of having three returns in a month and 100% matching invoices for verifying input tax credit has failed to take off. The monthly returns prescribed now does not have the details of input purchases and cannot be used to verify input tax credit. The annual return filing, that is supposed to contain the details to facilitate verification, has been repeatedly postponed and the last date prescribed now is March 31, 2021. In the absence of a verification mechanism, the GST has turned out to be a voluntary tax; with the fake invoice industry mushrooming, compliance has been low, providing a scope for inspector raj. This is mainly due to the failure to stabilise the technology platform. There cannot be any excuse for the technology service provider and the GSTN for not firming up the technology platform even after three years, and the GST Council must take up this issue on a priority basis.

There cannot be any excuse for the technology service provider and the GSTN for not firming up the technology platform even after three years, and the GST Council must take up this issue on a priority basis. There are press reports that the Council has discussed it with the service provider, but it is not clear when we will have the benefit of a robust technology interface. It is only when we have buoyant revenues that the reform of the structure of taxation becomes feasible.